IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX APPLICATION No 351 of 1999
with
TAX APPEALS NOS. 758 to 761 of 1999

For Approval and Signature:

Hon'ble CHIEF JUSTICE MR DM DHARMADHIKARI
and
Hon'ble MR.JUSTICE A.R.DAVE

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

COMMI. OF INCOME TAX

Versus

ATUL PRODUCTS LTD.

Appearance:
MR BB NAIK for MR MANISH R BHATT for Petitioner
MR JP SHAH for Respondent No. 1

CORAM : CHIEF JUSTICE MR DM DHARMADHIKARI
and
MR.JUSTICE A.R.DAVE

Date of decision: 02/02/2001

C.A.V.JUDGEMENT

(Per : MR.JUSTICE A.R.DAVE)

As legal issues involved in ITA No. 351/99 and in Tax Appeals Nos. 758 to 761 of 1999 are the same, at the request of the learned advocates, all the cases are heard together and are disposed of by this common judgment.

2. Learned Advocate Shri B.B. Naik has appeared for the revenue whereas learned advocate Shri J.P. Shah has appeared for the assessee in all these cases.

3. In ITA No. 351/99, which has been filed under the provisions of sec. 256(2) of the Income-tax Act, 1961 (hereinafter referred to as 'the Act'), it has been prayed by the applicant that the Income Tax Appellate Tribunal be directed to refer to this court the following two questions arising out of the order dated 12th May 1996 passed by the Income Tax Appellate Tribunal Ahmedabad Bench 'B' in I.T.A. No. 1843/Ahd/90, for its opinion.

1) Whether the Appellate Tribunal is right in law and on facts in confirming the order passed by the Commissioner of Income Tax (Appeals) deleting the addition of Rs. 2,93,56,000/- representing the alleged under valuation of closing stock?

2) Whether the Appellate Tribunal ought (not) to have appreciated that in absence of any cogent reason for change in the method of valuation such a switch over attracted the ratio of the decision of the Hon'ble Supreme Court in the case of McDowell & Co.?

3. For the sake of convenience, the facts involved in I.T.A. No. 351/99 have been narrated hereinbelow because the orders which have been challenged in the Tax Appeals filed by the revenue are based on the order of the Tribunal dated 12th May 1996, which is a subject-matter of I.T.A. No. 351/99.

4. The relevant facts pertaining to the case, which have given rise to I.T.A. No. 351/99, are as under :

5. The assessee, during the Assessment Year 1975-76, changed its method of valuation of stock. Prior to the said year, the assessee was valuing its material in process as well as finished goods on the basis of "cost price or market price whichever is lower", but during the Assessment Year, the assessee changed the method of

valuation and it started adding direct cost to the material in process and to the finished goods for determining its value. As a result of the change in the method of valuation of stock, the taxable income of the assessee had been reduced by Rs. 2,93,56,000/-. Applying the principle laid down by the Hon'ble Supreme Court in the case of McDowell & Co. v. CIT, 154 ITR 148, the Assessing Officer added the said amount to the income of the assessee while framing the assessment.

6. Being aggrieved by the addition of Rs. 2,93,56,000/-, the assessee preferred an appeal before the CIT (Appeals). The CIT (Appeals) allowed the appeal and directed deletion of the amount referred to hereinabove. The CIT (Appeals), while allowing the appeal, observed that in subsequent assessment years, the change made by the assessee in the method of valuation was accepted. Moreover, the changed method of valuation of stock was also in accordance with one of the accepted methods of accounting. The submission of the assessee that the change was made so as to have the method of valuation in parity with the method adopted by other companies doing similar type of business was also accepted by the CIT (Appeals).

7. Being aggrieved by the order passed by the CIT (Appeals), the revenue filed an appeal before the Income Tax Appellate Tribunal. The Accountant Member and the Judicial Member hearing the appeal differed and, therefore, the matter was referred to a third member. The Accountant Member agreed with the reasons given by the CIT (Appeals). In his opinion the Assessing Officer committed an error by adding the above referred amount to the income of the assessee, while the Judicial Member was of the view that the addition made by the Assessing Officer on account of changed method of stock valuation was justified. The third member, who was a Judicial Member, to whom the the matter was referred to, agreed with the view expressed by the Accountant Member and, therefore, on account of majority of the view expressed by the members of the Tribunal, the appeal filed by the revenue had been dismissed.

8. In the circumstances referred to hereinabove, the revenue submitted an application to the Tribunal for referring the questions referred to hereinabove to this Court, but, as the said application has been rejected by the Tribunal by an order dated 2nd February 1999, the Revenue has approached this Court under the provisions of sec. 256(2) of the Act with a prayer that the Appellate Tribunal be directed to refer the questions stated

hereinabove to this court for its opinion.

9. So far as Tax Appeals Nos. 758 to 761/99 are concerned, the impugned orders which have been passed by the Tribunal and which are subject matter of the said appeals are based on the Tribunal's order which is subject matter of I.T.A. No. 351/99. In the circumstances, we do not think it necessary to narrate the facts giving rise to the said appeals especially in view of the fact that the legal issue which has been involved in all the appeals and the I.T.A. is the same.

10. Learned Advocate Shri B.B. Naik appearing for the revenue has submitted that in all the cases there was an effort on the part of the assessee to reduce taxable income by undervaluing the stock. According to his submission, there was no justifiable reason for changing the method of stock valuation. He has relied upon the principles laid down by the Hon'ble Supreme Court in case of McDowell & Co. (supra). It has been submitted by him that there was an effort to reduce tax burden by the assessee by making a change in the method of valuation. He has also drawn our attention to the judgment delivered in case of CIT v. British Paints India Ltd., 188 ITR 44 and has submitted that the assessee should follow a consistent practice. According to him, by changing the method of stock valuation the assessee would not be showing its true income and therefore, in his opinion, the action of the Assessing Officer in each case should be upheld.

11. On the other hand, learned advocate Shri J.P. Shah appearing for the assessee has submitted that there was no intention on the part of the assessee to reduce the taxable income. According to him, there was a sound reason for changing the method of stock valuation by the assessee. It has been submitted by him that except the assessee, all other manufacturing units, which were doing similar type of business, were following the method which had been adopted by the assessee. Only the assessee was valuing its stock on the basis of "cost price or market price whichever is lower". All other business units doing similar type of business were adding all direct costs to the material in process and the finished goods for arriving at the valuation of material in process and finished goods. According to him, if the changed method was also one of the accepted methods of accounting and when all units in the same industry were following the method which was adopted by the assessee, there was no reason for the revenue to apply the principle laid down in the case of McDowell & Co. (supra) as there was no

intention on the part of the assessee to reduce its taxable income with an oblique motive. According to him, even the Accountant Member had come to the conclusion that behind the change in the method of stock valuation, there was no mala fide intention on the part of the assessee. Even the Judicial Member had not said that the change was with a mala fide intention. Thus, the tribunal had come to the conclusion that the change was bona fide. According to the learned advocate appearing for the assessee, if the change was bona fide and if the changed method was also a method which had been accepted as one of the sound accounting methods and as all other business units doing similar type of business were following the method adopted by the assessee, there was no reason for the revenue to have any doubt with regard to intention of the assessee and in that event the action of the Assessing Officer of adding the amount of difference in the income of the assessee was not justified and the majority view expressed by the Tribunal was absolutely just and proper.

12. Learned Advocate Shri J.P. Shah has relied upon the following judgments :

CIT, Tamil Nadu v. Carborandum Universal Ltd. 149 149 ITR 759

CIT v. Haryana Minerals Ltd., 242 ITR 704

CIT v. Ganga Charity Trust Fund, 162 ITR 612

CIT v. Delta Plantation Ltd., 114 CTR 271

CIT v. Dalmia Cement (Bharat) Ltd., 215 ITR 441

Kalpatta Estates Ltd. v. CIT, 221 ITR 601

13. We have heard the learned advocates at length and have also perused the judgments cited by them.

14. Looking to the facts of the case, so far as I.T.A. No. 351/99 is concerned, in our opinion, no question of law is arising out of the impugned order passed by the Tribunal. In our opinion, even the appeals filed by the revenue deserve to be rejected for the following reasons.

15. There is a finding of fact by the Tribunal to the effect that the change made in the method of stock valuation by the assessee was not with a mala fide

intention. Thus, it is very clear that only with a bona fide intention the assessee had changed the method of stock valuation. It is true that, as a result of the change made in the method of stock valuation, the taxable income of the assessee had been reduced. Any change in any method of stock valuation is bound to make some change in the taxable income. Simply because, by virtue of the change introduced by the assessee, the taxable income of the assessee had been reduced, by no stretch of imagination it can be said that the assessee had an intention to deliberately undervalue its stock so as to reduce its tax burden.

16. Thus, it is not in dispute that the change in the method of stock valuation is bona fide. It has been held by the Calcutta High Court in the case of CIT v. Delta Plantation Ltd., 114 CTR 271, that when the change is made by the assessee in the method of valuation of stock, so as to follow the method of stock valuation adopted by the entire industry, the revenue should not reject the method merely because there would be loss to the revenue in the year in which the method of stock valuation is changed. In the instant case, the method has been changed with a bona fide intention so as to have a method which was followed by the entire industry. Moreover, it has also been held by this court in the case of CIT v. Ganga Charity Trust Fund, 162 ITR 612, that when the accounting method is changed with a bona fide intention, the change should be accepted by the revenue.

17. Even the Delhi High Court has taken a view in the case of CIT v. Dalmia Cements (Bharat) Ltd., 215 ITR 441 that when the assessee changes its method of stock valuation and when there is a finding that the change was bona fide and when the changed method had been followed in the subsequent years, the Tribunal was justified in permitting the assessee to change the method.

18. Even the Madras High Court in the case of CIT, Tamil Nadu v. Carborandum Universal Ltd has held that if the method of stock valuation is changed and if the change is bona fide and the changed method has been continued, the difference arising in the income on account of the changed method is not includible in the income of the assessee during the relevant assessment year.

19. It is pertinent to note that even the Karnataka High Court has taken a view that when the method of stock valuation is changed and the change was bona fide, the change made by the assessee cannot be objected to by the

revenue.

20. Moreover, in CIT v. Haryana Minerals Ltd., the Punjab & Haryana High Court has also held that when there is a finding of fact to the effect that the change made in the method of stock valuation is bona fide, it is not open to the revenue to add any amount in the taxable income of the assessee which results on account of changed method of stock valuation.

21. Thus, looking to the law laid down by several High Courts on the subject-matter, it is very clear that if the method of stock valuation is changed by the assessee and if the change is bona fide, even if the taxable income is reduced on account of the changed method of stock valuation, it is not open to the revenue to add any amount in the taxable income of the assessee which is the resultant effect of the changed method of valuation.

22. We do not find any reason to deviate from the view which has been expressed by several High Courts including our own High Court. As stated hereinabove, it is not in dispute that the change was bona fide. The new method which was adopted has been continuously followed in the subsequent years. The assessee has changed the method so as to see that the method adopted by the assessee is also as per the method adopted by other business units in the industry. It is also pertinent to note that in the subsequent years the revenue had not objected to the change made by the assessee in the method of stock valuation.

23. Looking to the facts and legal position narrated hereinabove, we see no reason to entertain the application and the appeals. In the circumstances, I.T.A. No.351/99 is rejected and Tax Appeals Nos. 758 to 761 of 1999 are dismissed with no order as to costs.

(D.M. Dharmadhikari, C.J.)

(A.R. Dave.)

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